

Initiative 601: Experience and Context

Presentation to the House Finance Committee

by the

Office of Financial Management

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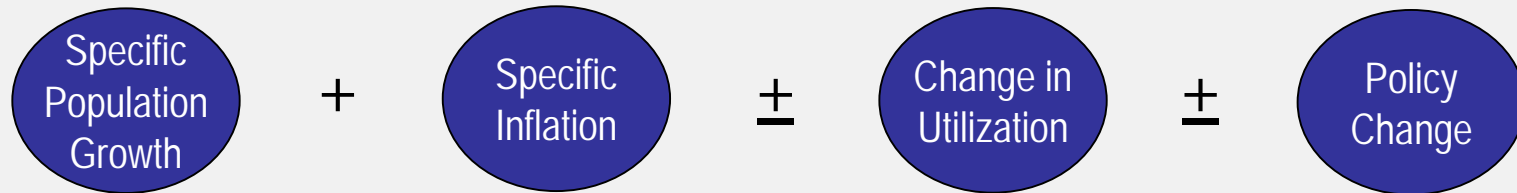
February 1, 2005

Major Provisions of I-601

- Establishes annual limits on General Fund state expenditure growth based on three-year averages of inflation and population growth, called “fiscal growth factors.”
- Under original I-601, the expenditure limit was reduced when program costs or revenues were shifted from the General Fund to other state accounts; but the limit could not be raised when such program costs or revenues were shifted back to the general fund.
- A new provision adopted in 2000 in HB 3169 allows adjustments in both directions. It establishes that the state expenditure limit can be adjusted upward when program costs or revenues are transferred to the General Fund from another state fund or account.
- Requires a 2/3 majority of both houses of the Legislature to increase revenues.

Components of Expenditure Growth

Budget Drivers =



EXAMPLE: MEDICAL ASSISTANCE

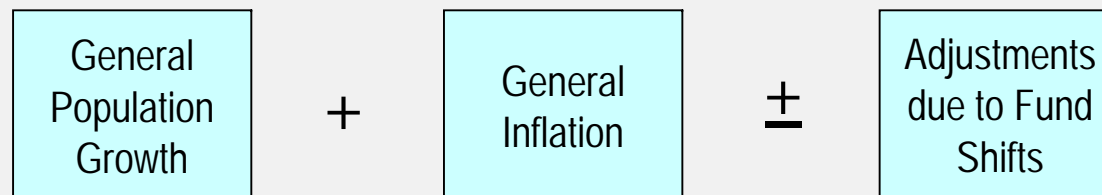
Ages 18 – 39
Females and
other age groups

Medical Services
Inflation

Factors Affecting
Enrollment
(e.g., Economy)

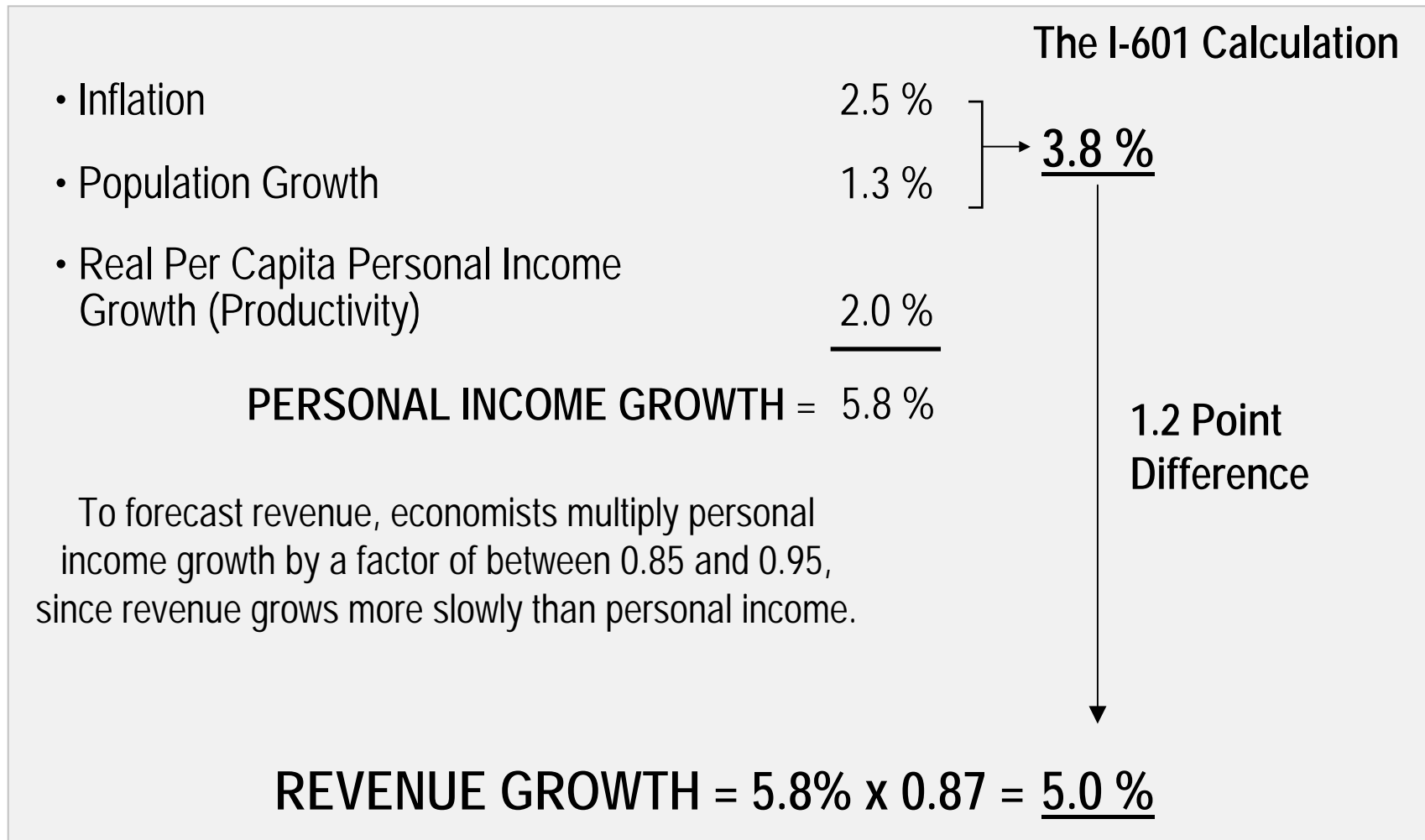
Changing
Eligibility
Criteria

I-601 Spending Limit =

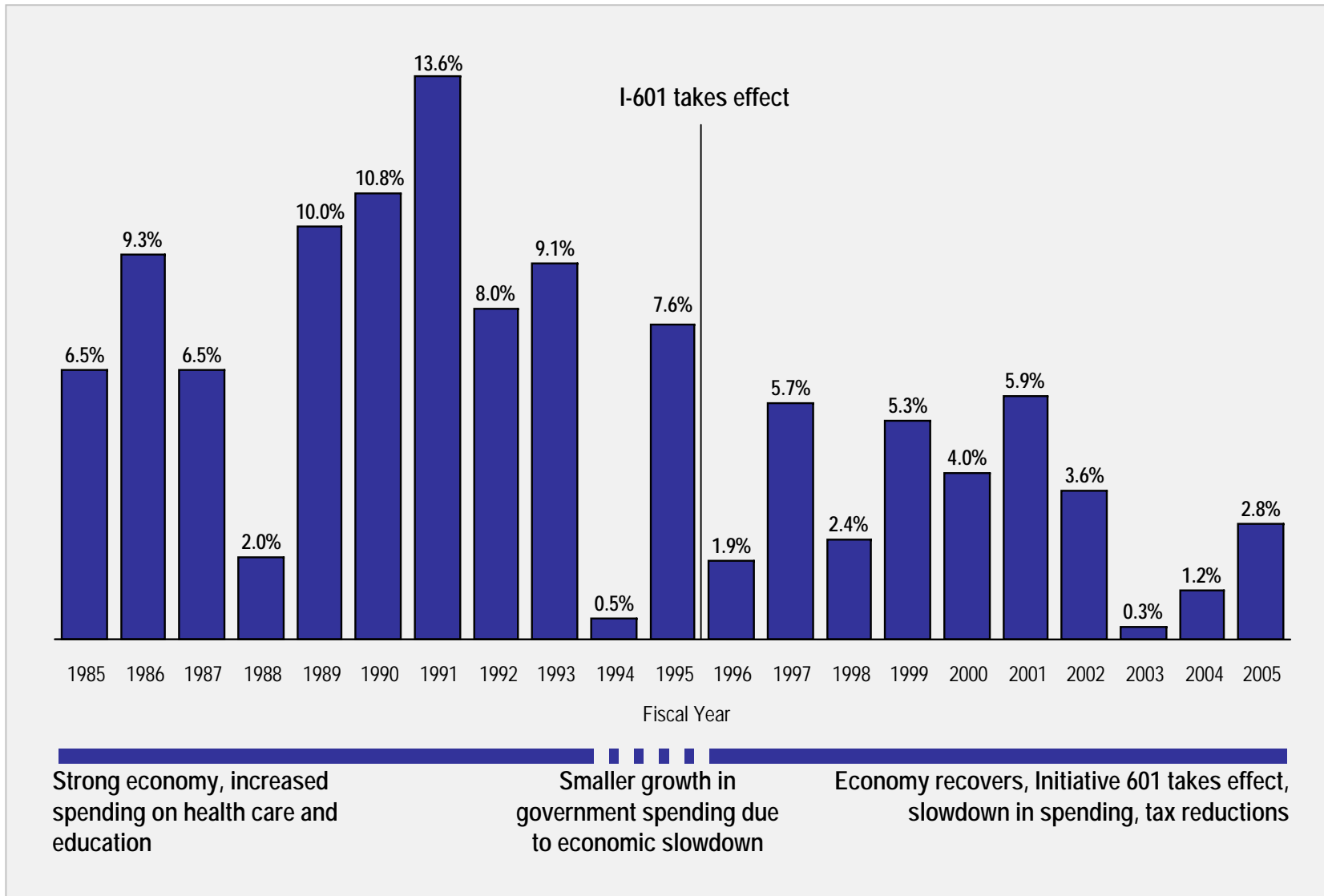


Structural Difference Between Revenue Growth and I-601

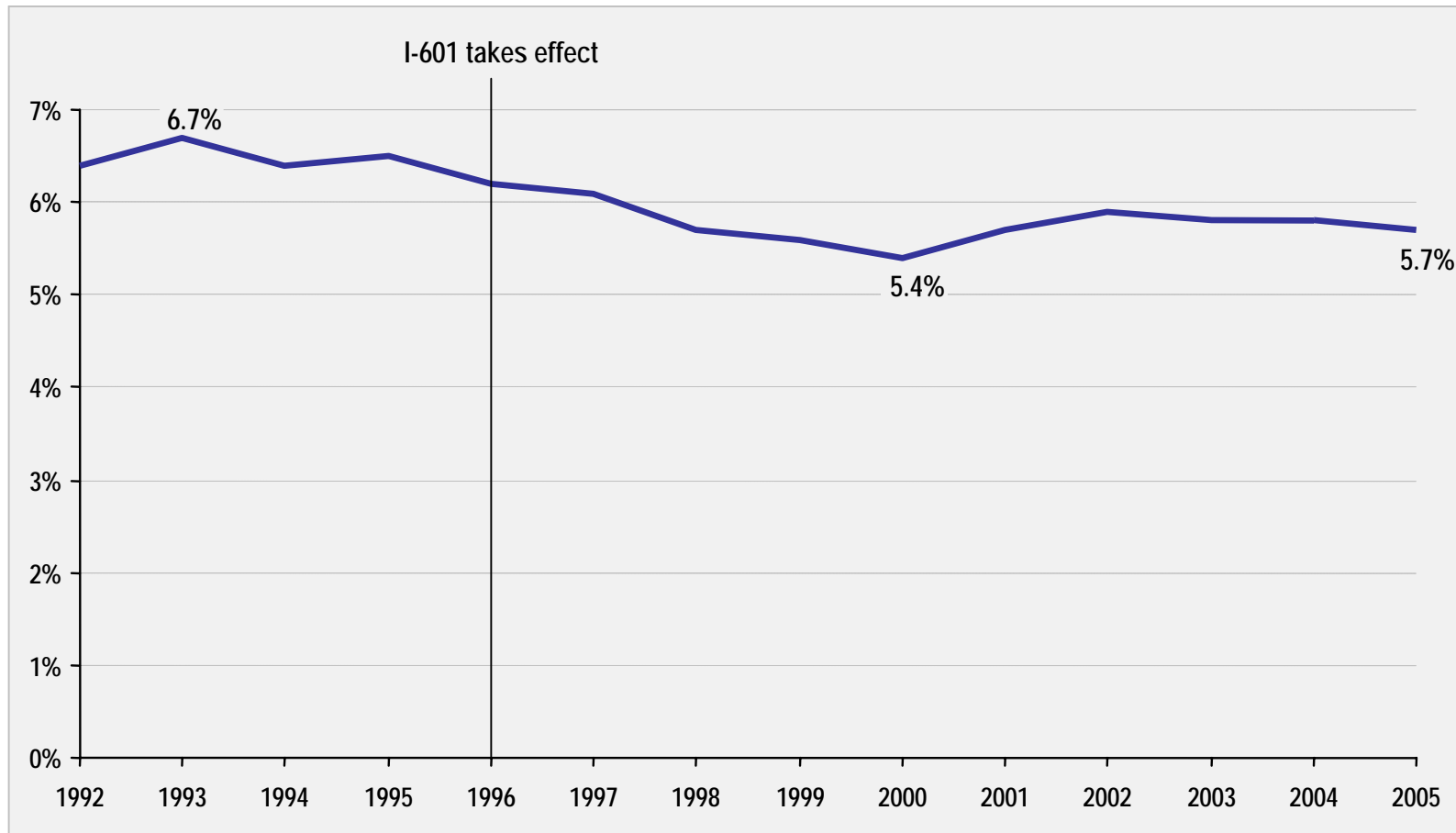
Average Projected Growth 2005 – 2009 (assumes average economic growth)



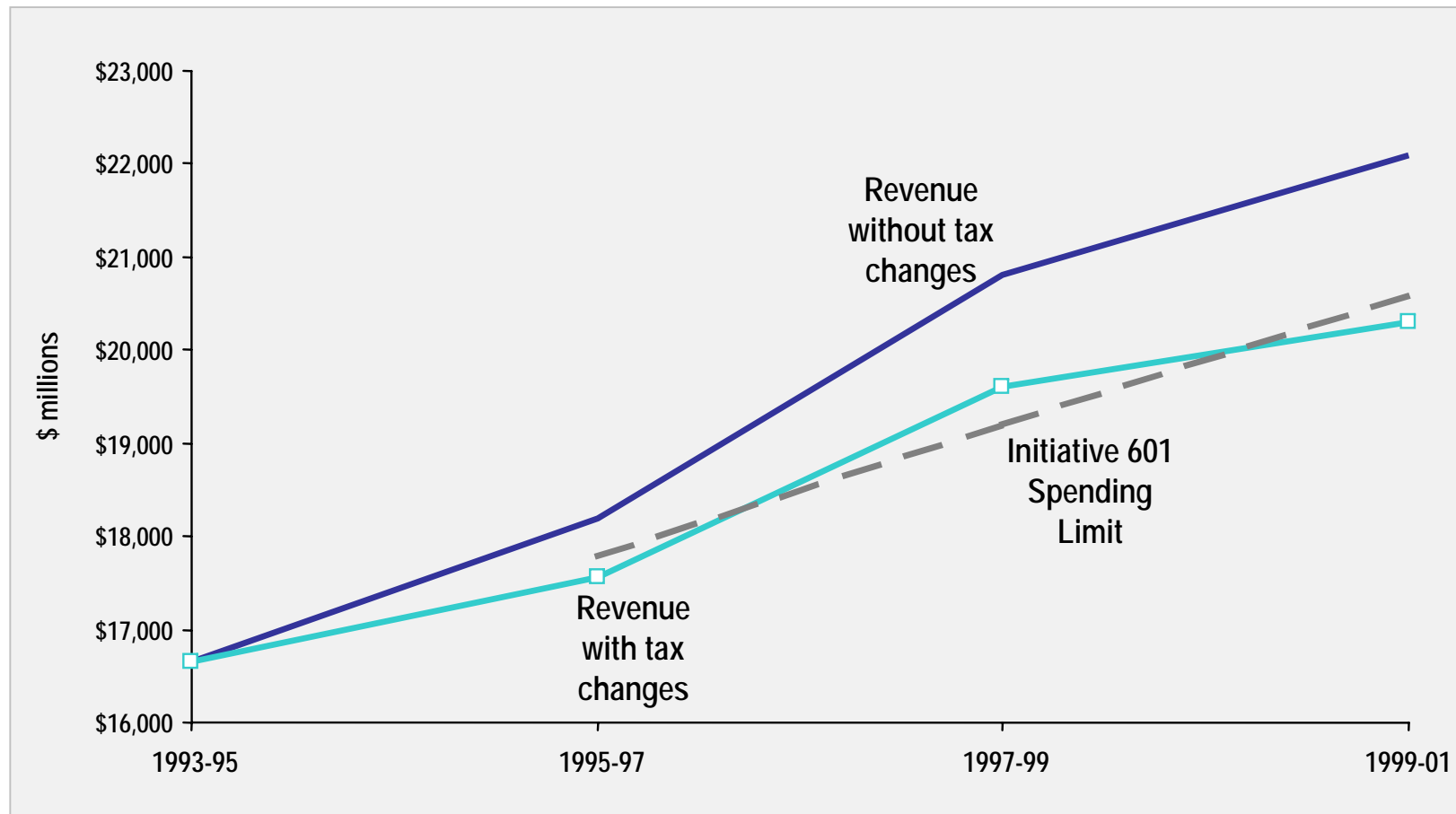
Growth in State General Fund Expenditures



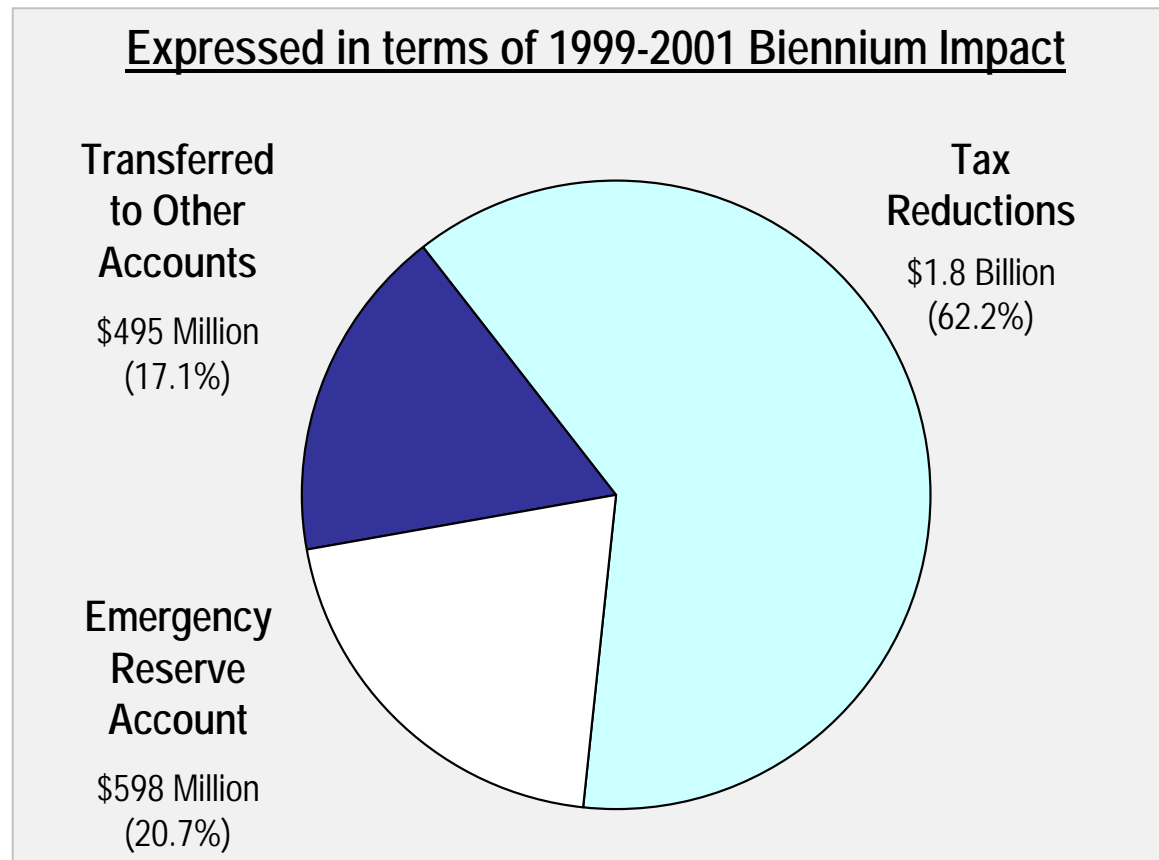
State spending as a percentage of total state personal income has declined since Initiative 601 took effect.



Tax reductions passed between 1994 and 2001 had the effect of reducing annual General Fund revenues to approximately the Initiative 601 spending limit.



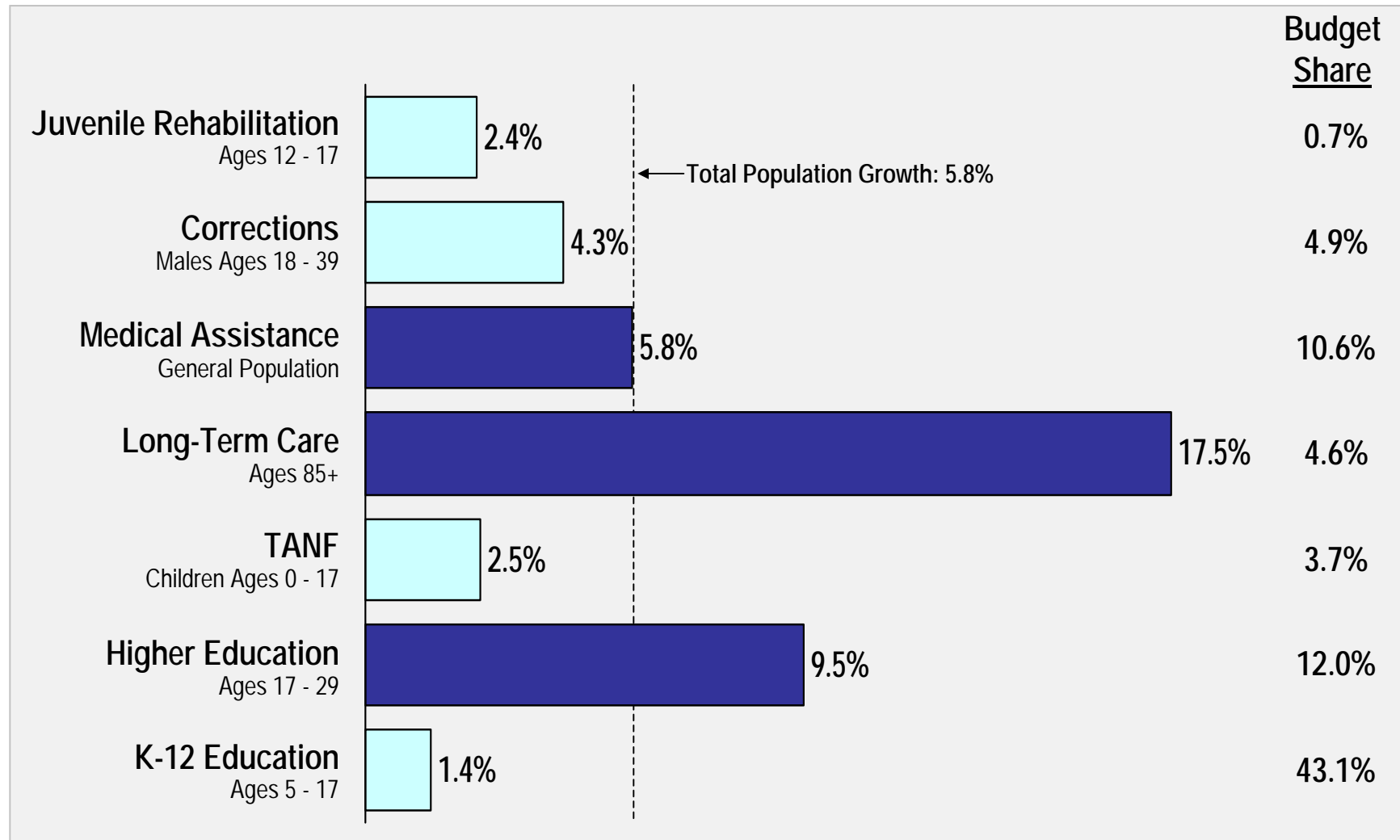
\$2.9 billion of unspent General Fund revenues was returned in the form of tax cuts, transferred to other accounts, or deposited in the rainy day fund.



Six factors that helped spending growth stay within I-601 constraints (through 99-01 Biennium)

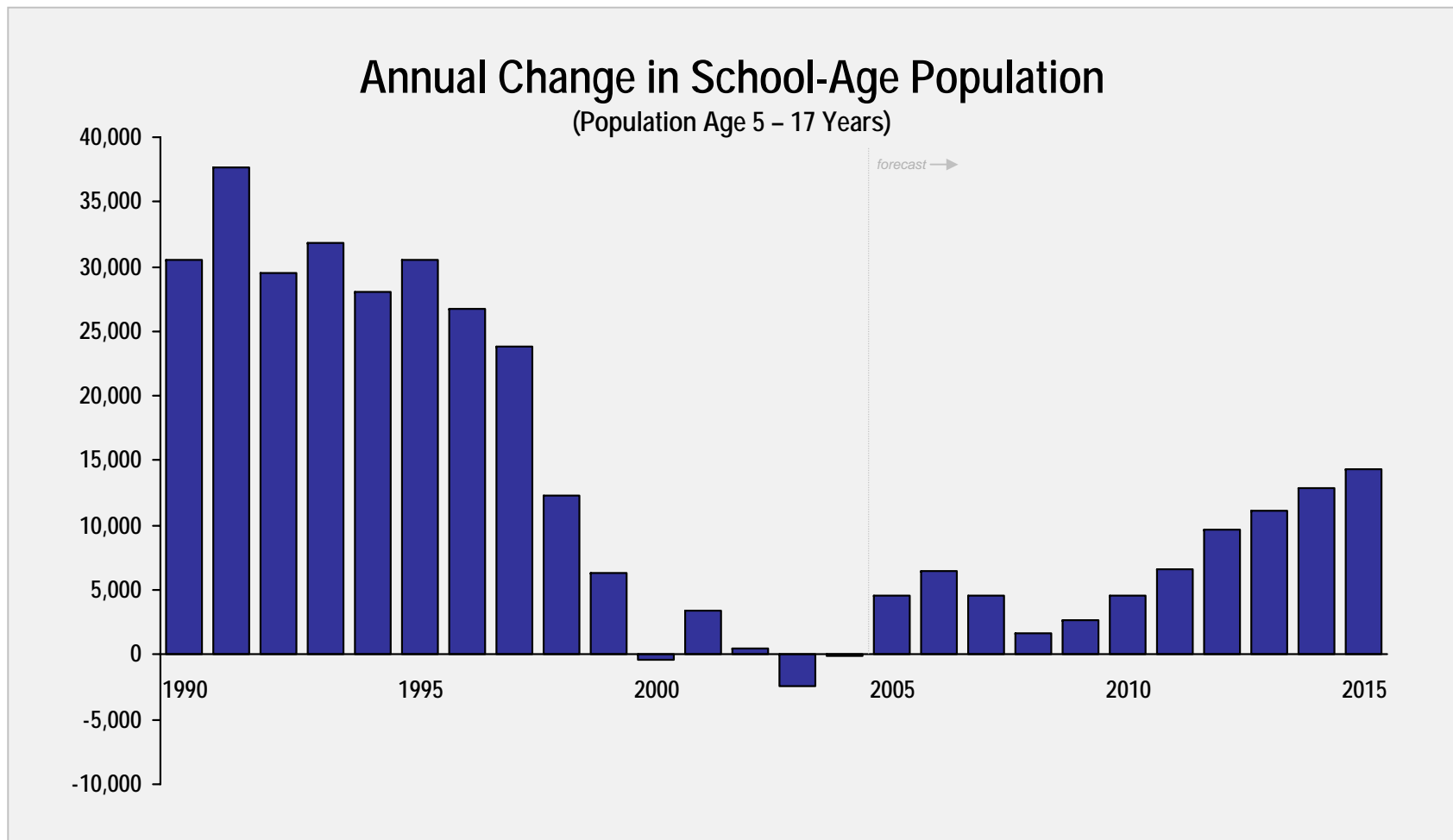
- Welfare reform, which substantially reduced caseload growth in the state's public assistance programs.
- Temporary reduction in medical services inflation and other cost savings in health care due to the introduction of managed care practices.
- Slowdown in salary growth for state employees.
- Additional, unexpected one-time revenues (e.g., the "tobacco settlement") which helped fund health care programs outside the general fund.
- Favorable investment climate which (at least temporarily) reduced public contributions to state pension funds.
- Flat growth in K-12 enrollment.

Projected Change in Budget Driver Populations 2003 - 2007



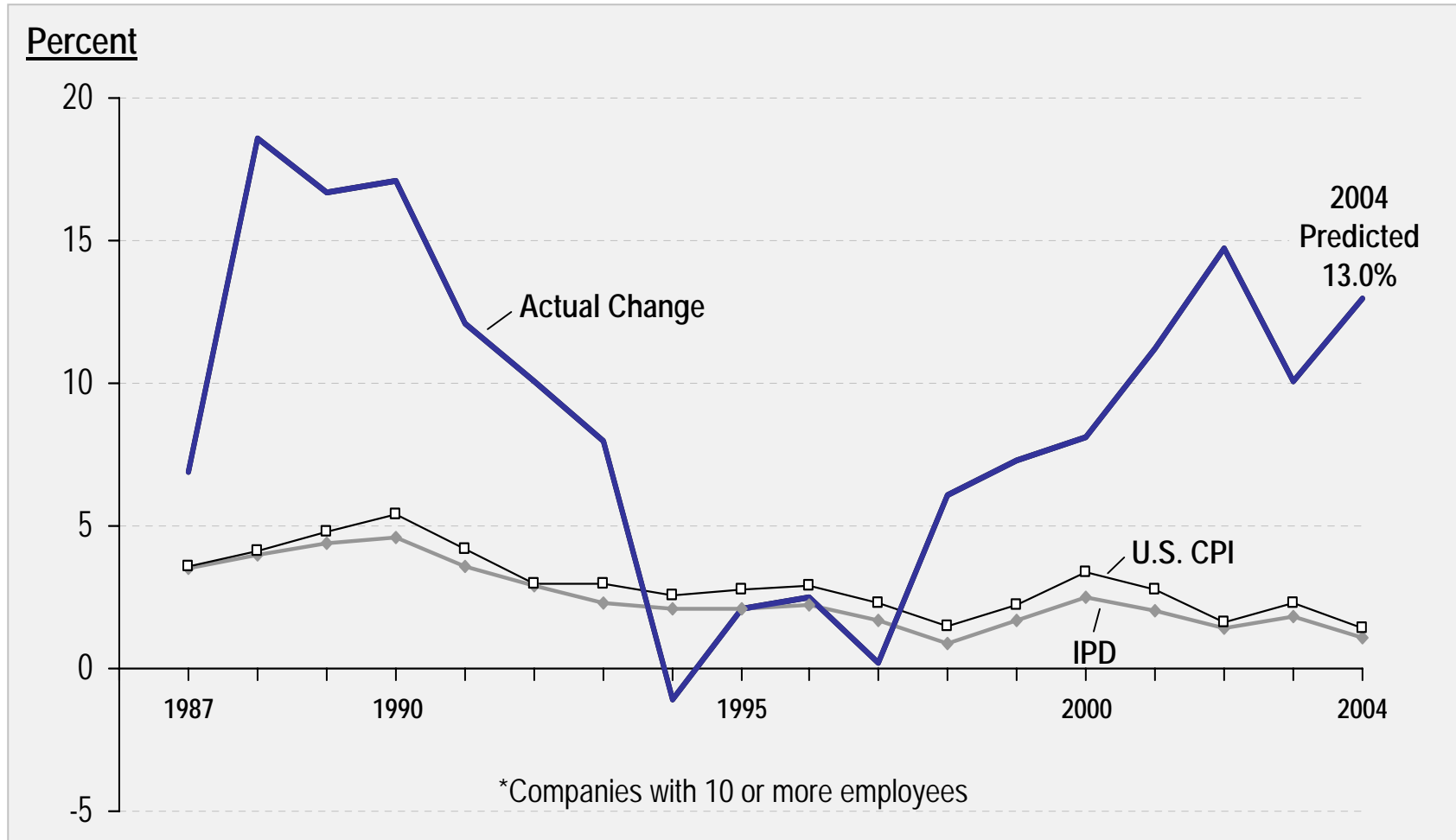
Source: OFM November 2004 State Population Forecast

However, K-12 enrollments are forecast to surge again after 2008.



Percent Change in Employer Medical Costs

Per Employee*



Sources: Mercer National Survey of Employer-Sponsored Health Plans 2003, Global Insight, Office of Financial Management

In addition to health care “inflationary” pressures, policy pressures across several major programs are high.

	Percent of Budget	Demographic Pressures	Inflation Pressures	Policy Pressures
Higher Education	12.3	High	High	High
K-12 Education	43.5	Low*	-----	High (class size, COLAs)
TANF	6.8	Low	-----	-----
Medical Assistance	9.5	High (aging of the population)	Very High	High
Long-Term Care	4.6	High	-----	-----
Prison	5.3	Low	-----	-----
Juvenile Rehabilitation	0.8	Low	-----	-----
*Demographic pressures for K-12 will begin to accelerate in FY 09.				

Fiscal Outlook

2004 – 2009

(Builds on 2003-05 Supplemental Budget as passed in April 2004)

	Scenario 1	Scenario 2
Employee COLAs IPD	X	X
Caseload growth – based on official caseload forecasts where available OR Growth in associated population group	X	X
General inflation (goods and services): IPD – 2.2 %	X	X
Higher education maintains its 03-05 participation rate.	X	X
No other policy adds are included.	X	X
Annual growth in per capita health care costs :	IPD 2.2%	10%
Growth in pension contributions :	IPD 2.2%	State Actuary's Estimate*
*not including gain-sharing		

Scenario 1: All programs, including health care costs and pension contributions, grow based on caseload/specific population growth and general inflation. Revenue grows 5% annually.

			PROJECTION			
	2004	2005	2006	2007	2008	2009
Total Revenues & Resources	\$11,531	\$11,882	\$12,077	\$12,698	\$13,190	\$13,824
Total Expenditures	\$11,452	\$11,994	\$12,400	\$12,759	\$13,118	\$13,369
DIFFERENCE	\$79	(\$113)	(\$323)	(\$60)	\$72	\$455
TOTAL RESERVES/DEFICIT*			(\$257)	(\$397)	(\$440)	(\$121)

Result: Revenue almost keeps pace with budget pressures.

Scenario 2: Same as Scenario 1 except health care annual cost per case growth is 10 percent and pension contributions are based on State Actuary's estimates.

			PROJECTION			
	2004	2005	2006	2007	2008	2009
Total Revenues & Resources	\$11,531	\$11,882	\$12,077	\$12,698	\$13,190	\$18,824
Total Expenditures	\$11,452	\$11,994	\$12,834	\$13,462	\$14,293	\$14,899
DIFFERENCE	\$79	(\$113)	(\$757)	(\$764)	(\$1,102)	(\$1,076)
TOTAL RESERVES/DEFICIT*			(\$690)	(\$1,534)	(\$2,751)	(\$3,962)

**Result: Revenue does not keep pace with budget pressures.
Deficit is difficult to manage.**

Projected Annual Growth

